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Business in Brief

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THE CHASE MANHATTAN BANK

The economy may pass the $400 billion milestone in the current quarter. Yet the pace of the rise in business activity is slowing.

Some leveling in the upward business curve was inevitable as the expansion moved into a mature stage. Production had begun to press against capacity in the fourth quarter. So a continued rapid increase in demand could only bring rising prices.

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However, several key factors have combined to level out the advance in over-all demand:

- **The Federal Government is running a cash surplus** that is siphoning purchasing power out of the private economy at a rate of $4-5 billion a year;
- **The Federal Reserve Board's policies** are restraining the rise in money and credit;
- **Consumer markets are becoming less bouyant**—in large part because of lower auto and housing sales.

Meantime, four of the major forces behind the expansion are continuing to exert an upward thrust:

- **Business investment** in new plants and equipment is up more than one-fifth in the past year and surveys point to a continued advance;
- **Consumer incomes** are rising—so that consumer markets are still generally strong, despite the slowdown in autos and a rise in instalment debt repayments;
- **State and local government** expenditures show an upward trend, chiefly for public works.
- **Buying to replenish inventories** added to over-all demand at a rate of about $6 billion in the last quarter. That's about twice the rate of increase needed to keep pace with the normal growth of sales.

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Up to now, the factors pushing activity upwards have outweighed the restraining factors. However, over-all activity is likely to rise at a rate of less than $4 billion in the current quarter. In the previous year it went up $8 billion a quarter. Thus, the forces making for restraint have been gaining strength.

Several significant changes in economic trends are in the making.

- The Federal Government is planning to spend more—on defense, foreign aid, schools, roads, medical research and farm programs;
- A cut in Federal taxes will be given consideration;
- Restrictions on mortgage credit have already been eased somewhat, and the Federal Reserve Board is alert to any shifts in business trends;
- Major style changes in the 1957 autos may strengthen sales later in the year.
- In contrast to these potentials for expansion, the rate of inventory building is bound to slow down.

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In short, the economic picture promises to show mixed patterns as we move through 1956. Readjustments are underway, or clearly in prospect, in a number of important areas. Despite the great underlying strength of the economy, these adjustments are bound to have an impact on general business activity.

The fact that some readjustments lie ahead is supported by recent behavior of the National Bureau of Economic Research indicators. The latest reading of the indicators suggests that a peak in the current business cycle may not be far distant. These indicators merely point to a change in trend—they do not show the extent of the possible change in direction.

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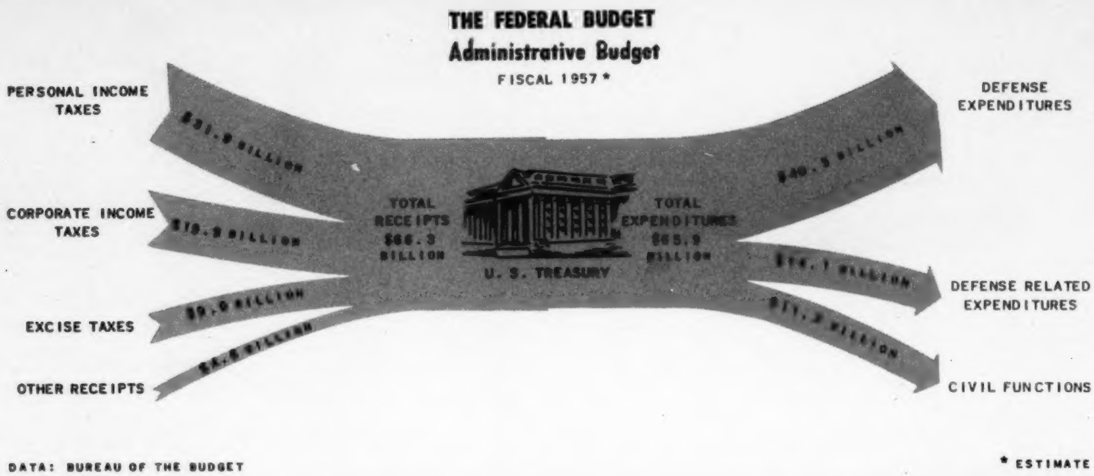
However, the significant thing is that the over-all impact of the readjustments that can now be foreseen promises to be mild. The long-term forces making for economic advance continue unabated. Rapid population growth, rising productivity and a steady broadening of consumer markets are the dominant features of our economy.

With this firm underpinning, it should be possible to handle the adjustments that appear to lie ahead without serious trouble. Thus, 1956 is likely to see a leveling of the business curve—it can be a period of consolidation of past gains and of preparation for a renewal of sound economic growth.



THE BUDGET

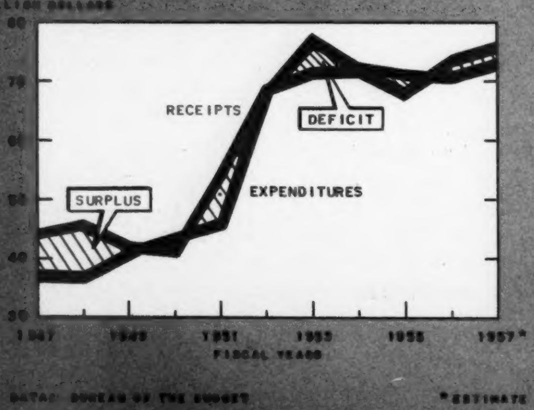
Continued Economic Growth Will Greatly Ease the Budget Problem

The President's budget message marks a dramatic turning point in the recent history of Federal budget policy. Its significance can be briefly summed up in these terms:

1) The budget has finally been balanced. When the Administration took office, it faced a deficit of $9.5 billion. Since then:

- Taxes were cut $7½ billion in 1954 to cope with the recession;
- But national income has been rising, so actual tax revenue is now almost as large as in 1953.
- Meanwhile, the Administration has cut expenditures enough to balance the budget.

2) The budget picture should continue to improve. Tax revenues could increase very substantially in the next five years—assuming no change in tax rates and continued growth in the economy. Expenditures promise to grow more slowly.



3) However, the Budget Message does not recommend tax cuts at this time. Because business activity is at a record level, the Administration feels a policy of budget restraint is in order.

Administrative Vs. Cash Budget

Why does a balanced administrative budget amount to a policy of moderate restraint on the economy? For an answer, it is necessary to distinguish between the administrative and the cash budget. The conventional or "administrative" budget excludes operations of the social security trust funds and certain other transactions.

The cash budget, in contrast, includes these items. It covers all receipts from, and payments to, the public. Thus, the cash budget is a better measure of the government's impact on the economy. Here is how the administrative and cash budget figures compare for fiscal 1957 (July 1956–July 1957):

	Billions of Dollars		
	Receipts	Expenditures	Surplus
Administrative Budget	$66.3	$65.9	$0.4
Cash Budget	75.4	72.9	2.5

When the government runs a cash surplus, it withdraws more from the private spending stream (by taxes) than it puts in (by expenditures). Consequently, it tends to hold back private spending. When the government runs a cash deficit, it does the reverse.

Why Restraint is in Order

Why does the Administration believe a policy of budget restraint is in order at the present time? There are two main reasons:

In the first place, the economy is now operating at close to full capacity. So long as this is true, a cash surplus is needed to help contain inflationary pressures.

Increases in the over-all demand for goods and services must be held down to the 3-4% per year growth in the economy's total production.

Secondly, it is necessary to balance the budget and accumulate a cash surplus in prosperous times to maintain fiscal integrity. It is always easier to appropriate than to tax. Thus, it is important to balance the budget over the business cycle. Only in that way can expenditures be put to the traditional test of whether they are worth their cost in taxes.

Fiscal Policy and Business Cycles

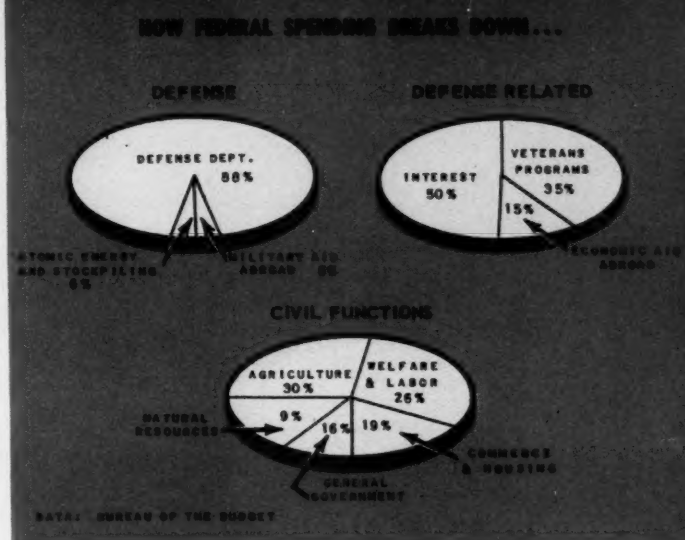
Wise and responsible fiscal policies have an important role to play in both prosperity and recessions. Recent experience illustrates this point. In fiscal 1955 Federal cash payments exceeded receipts by $3 billion. Thus, the cash deficit contributed to the recovery from the 1953-54 recession.

The remarkably rapid recovery during fiscal 1955 lifted gross national product 8%—more than double the long-term growth rate of our economy.

Since production was approaching capacity as fiscal 1956 began, the problem was to slow down the rise in spending throughout the economy. Otherwise, spending promised to rise faster than production, placing inflationary pressure on prices.

Near-Term Budget Problems

The shift to a cash budget surplus has helped stabilize our economy. For fiscal 1956 as a whole, Federal financial operations will siphon $2.5 billion of purchasing power out of the private economy. Thus, the swing—from a $3 billion deficit a year ago to a $2.5 billion cash surplus—amounts to potent anti-inflationary medicine.



At the present time, the business curve shows some signs of leveling out. If these trends continue, pressures for tax cuts will multiply. However, to maintain fiscal responsibility the burden of proof should be placed on those who argue that tax reduction is necessary to support sound growth in the economy.

It is, of course, true that the present level of Federal taxes is burdensome. Moreover, long-term budget prospects indicate that we may well be able to reduce tax rates during the next five years.

However, in working toward the broad objective of keeping our economy on a reasonably even keel over the years ahead, it is important to hold the line against tax reduction in times of high-level business activity. The potent expansionary force of tax reduction should be held back until there is a clear need for its use.

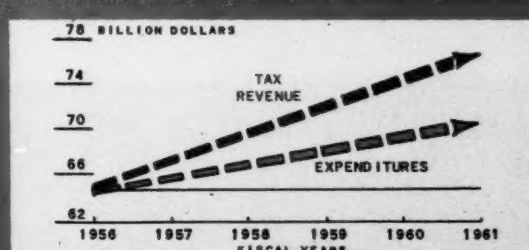
LONG-RUN BUDGET PROSPECTS

Long-run budget prospects seem excellent. Here is how trends might shape up for the next five years:

¶ Assuming no change in tax rates and a 3½% rate of economic growth, tax revenue could increase at least $12 billion by fiscal 1961.

¶ Expenditures will probably rise to support our growing economy. But the increases should add up to no more than half the rise in revenue:

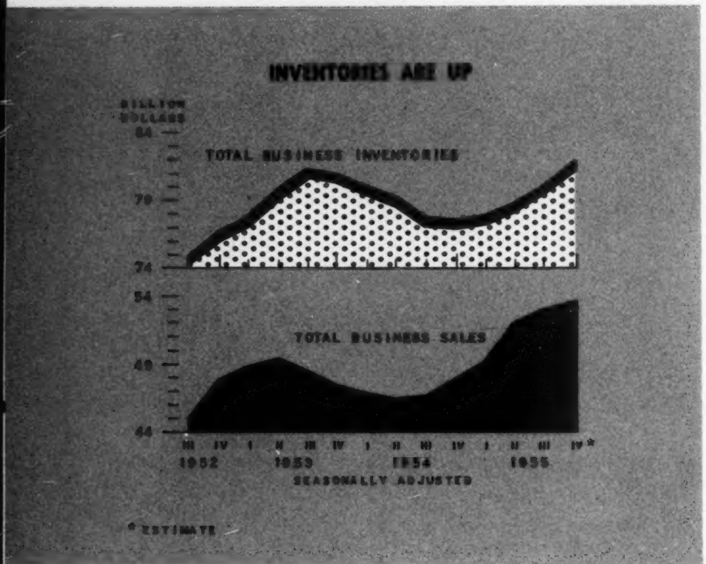
- Defense spending may rise—in part because "technological break-throughs" will make weapons more costly. Barring dramatic changes in the cold war, however, the increase is not likely to exceed $2-3 billion a year.
- Foreign economic aid may edge up a bit.
- Federal aid for roads and schools, and spending under the farm program, probably will increase. But an added $2-3 billion a year should cover all essential programs here.



¶ Consequently, there is a good chance that we shall be able to support necessary increases in expenditures, make moderate tax reductions and have a balanced budget in prosperous years.

INVEN

They Are Growing Rapidl ut Are



① INVENTORIES are building up. They have been expanding recently at an annual rate of \$5-6 billion—the fastest rate since 1953. However:

- Stocks are barely back to their 1953 peak.
- Business sales are 8% above their 1953 peak.

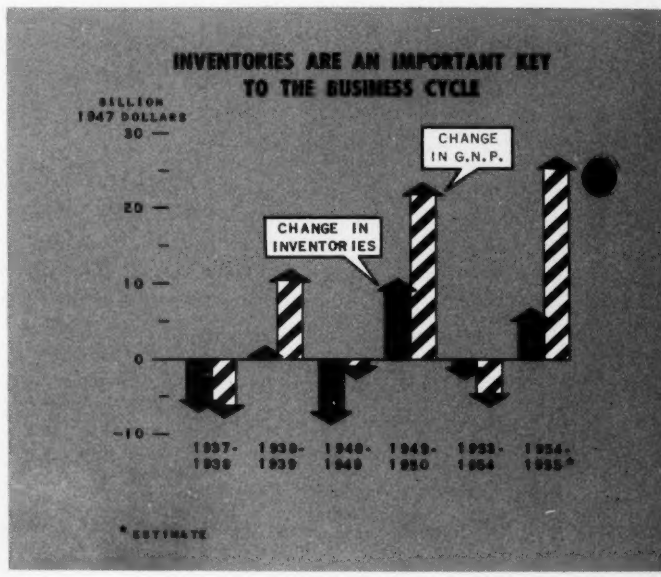
Thus, inventories are sound in relation to current sales.

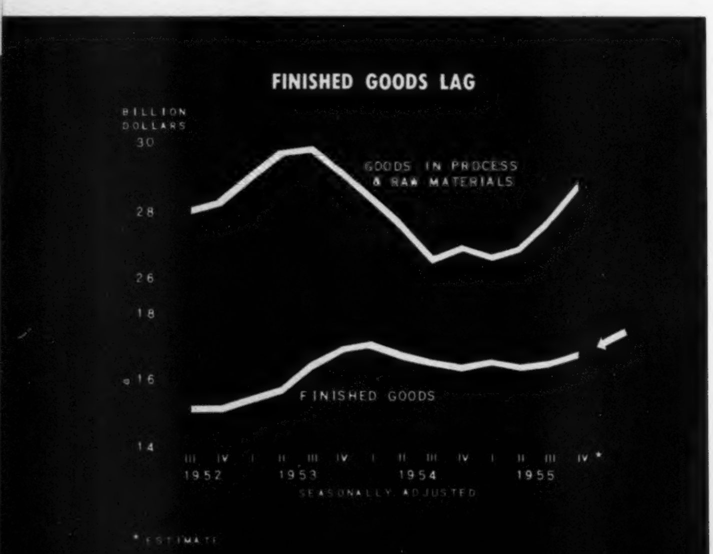
But inventories would become excessive if the recent rate of increase continued for long. To support the normal growth in sales, inventories should rise about \$3 billion a year.

② INVENTORY CHANGES play a crucial role in the business cycle.

- Increased inventories have accounted for nearly one-fifth of the total rise in national production in nine periods of expansion since 1918.
- And inventory liquidation has made up more than half the reductions in output during periods of business decline since 1918.

Consequently, although inventories do not seem dangerously high as yet, they'll bear careful watching in the period ahead.



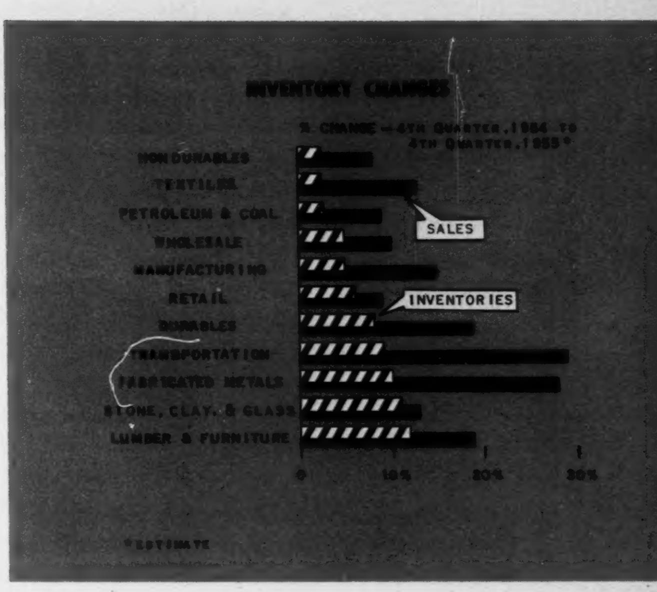


③ MOST OF THE INVENTORY RISE in manufacturing occurred in goods in process and raw materials. Goods in process are up \$1.3 billion in the year ending November 30, 1955. Raw materials are up \$0.7 billion. These increases are closely tied to the growth in business sales.

FINISHED GOODS, meanwhile, have risen about \$300 million. Since speculative excesses usually show up in finished goods, the rise so far does not appear to have featured much speculative accumulation.

ENTORIES

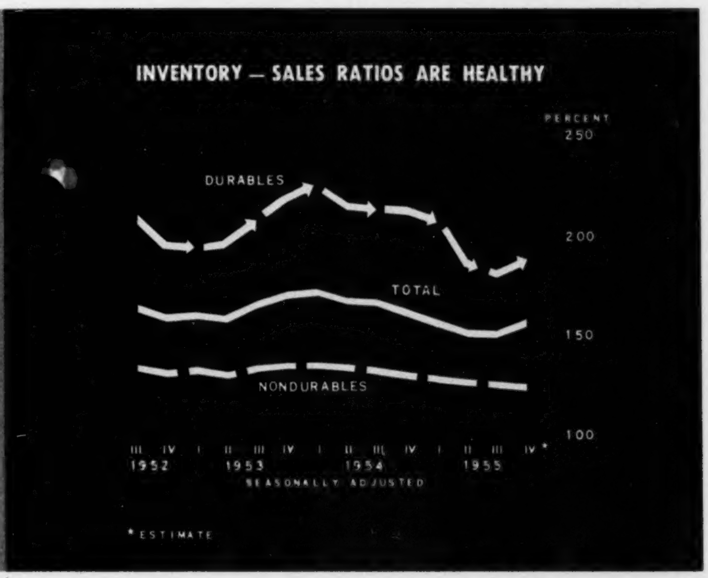
t Are Sti[illegible]n Line with Current Sales



④ THE GREATEST GROWTH in inventories has occurred in areas of the economy with the largest rise in sales.

THE CONSTRUCTION BOOM, for instance, has lead to an expansion in stocks of lumber, stone, clay and glass products. Last year's spectacular rise in auto sales has caused an increase in inventories in that industry.

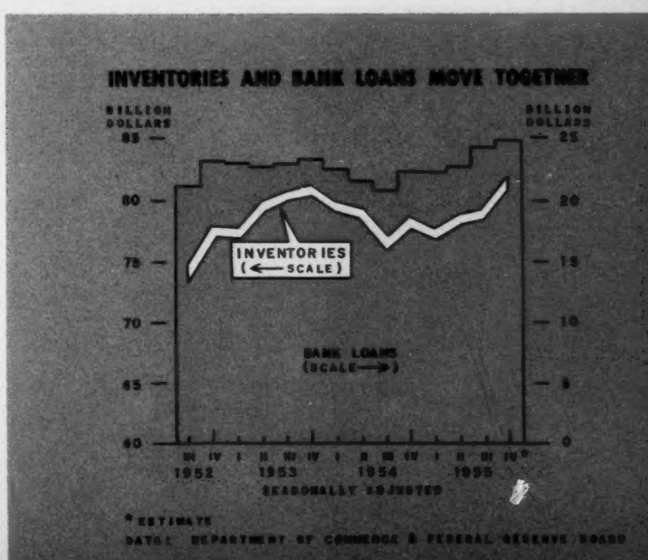
At the retail and wholesale level, stocks were up nearly 6% in the year ending last November 30th.



⑤ STOCK-SALES RATIOS were generally moderate at the end of November because inventory investment had lagged behind increased sales. Inventories grew faster than sales in late 1955. But there was room for some rise—inventory-sales ratios were below the levels of 1953 and 1954.

⑥ BANK LOANS and inventories generally move together. Banks are now in a period of seasonal decline for loans to food manufacturers and commodity dealers. A big question in the loan outlook, however, is whether inventory accumulation in other lines will continue to generate additional demand in the first quarter.

Sometime in 1956 inventory accumulation seems likely to slow down. Meanwhile, the policy of credit restraint followed by the Federal Reserve Board is directed toward curbing undue inventory accumulation as well as other credit extremes.



LEISURE

Will More Free Time Mean Less Output?

The American people have more time on their hands than ever before. Shorter hours, earlier retirement, longer vacations, the two-day week-end—all have brought dramatic changes in our way of life. Past trends show that:

• In the last hundred years the average workweek has dropped from 65 to 40 hours a week.

• Less than a quarter of the people over 65 years of age work today – compared with nearly 40% in 1900. The average period a worker can expect to spend in retirement has doubled—from three years in 1900 to six years today.

• In addition, most workers now take a two week paid vacation. In 1900, the average vacation was less than one week.

However, increased leisure has not unduly retarded the pace of economic growth. The really remarkable fact is that we have enjoyed both of them.

Leisure and Growth

Why hasn't increased leisure cut back economic growth? One reason is that people live longer today. Working life expectancy has increased from an average of 39 years in 1900 to 43 years today. Increases in longevity have raised the average number of working years enough to offset in part the effects of earlier retirement and later entry into the labor force.

More important, productivity has been rising very rapidly—and a good deal more rapidly than increases in leisure. As a result, people have been able to divide gains in productivity between leisure and higher income.

Of the total increase in productivity since 1870, about 65% has been taken in the form of higher income, while 35% has been taken as leisure. Since 1929, a 60-40 ratio has prevailed.

Leisure Markets

Increases in leisure have had further important consequences. For example, they have created a soaring market for leisure goods.

Americans spend about $32 billion a year in the leisure market today. Of this, we spend:

• Nearly $10 billion a year on vacations and week-ends. (A record $1.5 billion was spent on foreign travel alone in 1955.)

• Nearly $3 billion is spent on radio, TV, and musical instruments.

• $2.5 billion on toys and sports equipment.

• And $2 billion on movies, plays, and spectator sports.

Leisure markets should exceed $37 billion by 1960.

In addition, the demand for leisure in old age has contributed to a striking increase in saving to provide for old age security. In the short span of 10 years, for example, the number of private pension plans has tripled.

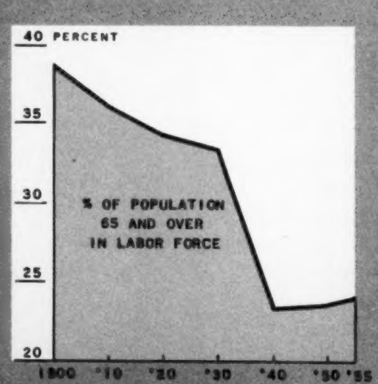
Future Trends

The average American is not likely to reverse his preference for more leisure. In all probability, he will continue to divide his gains in productivity into about two-thirds more income and one-third more time to enjoy the benefits of rising income.

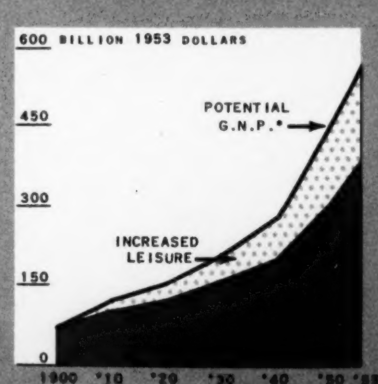
Thus, if productivity continues to increase at its long-run rate, the average American can realize his preference for leisure—in 25 years the 35 hour work week may be within reach. And, at the same time, production could continue to grow as fast—or faster—than in past decades.

PEOPLE WORK SHORTER HOURS

...AND RETIRE AT AN EARLIER AGE



...STILL OUTPUT AND LEISURE HAVE RISEN TOGETHER



DATA: DEPT. OF LABOR, DEPT. OF COMMERCE AND W. LEONTIEF

*ASSUMES HOURS WORKED/WEEK AND RETIREMENT AGE OF 1900

ECONOMIC STATISTICS

Why the Economic Pulse-takers Need Better Information

Mark Twain, having listened to widely-varying estimates of the length of the Mississippi River, once marveled at "The fascination of a science where one gets such wholesale returns of conjecture out of such a trifling investment of fact".

Only a quarter century ago, the same could be said of economics. The subject dealt heavily in abstractions and was short on actual facts against which to check its theories. Economists often disagreed because they had no accurate measurements.

In recent years, however, some important forward steps have been taken. Among other matters, economists have devised new and better methods for measuring the trends of our economy. As a result, the Federal Government spends about $40 million a year on compiling economic statistics today.

Where the Money Goes

What do we get for this sum? In the first place, we get much more detailed information on trends in the economy. Detailed statistics on production, employment and sales, for example, are useful to individual industries and firms in managing their business.

Secondly, this large and growing body of economic intelligence has been molded into an analytical framework which shows how various parts of the economy fit into the whole. National income statistics, for example, measure the total output of the economy, and the importance of each major component.

These statistics provide essential guide-lines for the formulation of economic policy. It is impossible to gauge the impact of changing credit policies on inventories, for example, without accurate measurements of how much inventory build-up is taking place.

A third aspect of the problem of mapping economic trends is the recent development of surveys of what consumers or businessmen plan to do in the period ahead. The most important of these are the McGraw-Hill and the Department of Commerce surveys of businessmen's plans to invest in plant and equipment, and the Michigan Survey Research Center's surveys of consumer plans to spend.

These surveys have made vital—but still limited—contributions to the economist's ability to forecast the future.

Shortcomings in Economic Statistics

But impressive though our progress has been, some important shortcomings remain. During the last six months, a group of business and university experts has made a careful review of the current state of our economic knowledge under the auspices of the Federal Reserve Board and the Joint Committee on the Economic Report.

Their findings point to a number of weaknesses in our current data which all users of economic statistics should be conscious of. Among the more striking of these are:

- Inventory statistics—which are based on a surprisingly small sample of total inventories. Since inventories play a key role in the business cycle, (see page 4) better statistics here are highly desirable.
- Construction statistics—also based upon inadequate and fragmentary samples of total construction activity.
- Savings statistics—which are generally derived by subtracting consumption from income.

Urgent Needs

In addition, there is needed more and better data on *future* intentions to spend. Only $100,000 a year is spent in surveying consumers intentions to spend. A larger and more intensive sample here could lead to more accurate predictions of spending by this pivotal sector of the economy. We also need surveys for inventories and construction.

The Joint Committee has urged increased appropriations for economic statistics. The $40 million that the government spends on statistics today is only a tiny fraction of Federal expenditures. A small increase here —on the order of $5 million—could pay very large dividends in providing the economic intelligence needed to help keep our economy prosperous and growing.